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C O N F I D E N T I A L SECTION 01 OF 03 MOSCOW 005784

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SUBJECT: GREF CENTER'S VIEWS ON RUSSIA'S ECONOMIC DIRECTION

REF: MOSCOW 2527

Classified By: Ambassador William J. Burns. Reasons: 1.4 (b, d).

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Summary  
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11. (C) In a December 6 meeting, Ksenia Yudaeva, Director of Research at the Center for Strategic Research (CSR or the Gref Center), the economic brain trust for the GOR's economic reforms in the early years of President Putin's administration, told econoff that while reform momentum has slowed the Center remains influential. She said the Center's current projects include preparing the Ministry of Economic Development and Trade's (MEDT) long-term economic strategy paper, preparing regional economic development strategies for Minister of Regional Development Kozak, and conducting research for Sberbank and the newly created Development Bank. Yudaeva appeared resigned to the current GOR reliance on state corporations as a model of economic policy and may be pinning her hopes on CSR's contacts in the GOR to lobby against the excesses of state intervention in the economy. She said that inertia will most likely characterize GOR economic policy for some time following the March 2008 presidential elections. End summary.

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Gref Center Stays Plugged In  
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12. (SBU) Yudaeva said that when Putin became prime minister in 1999, he established the CSR, with GQman Gref as its head, to develop an economic reform program and put thQ Russian economy onto a market path. (N.B. Gref went on to head MEDT until the cabinet reshuffle in October and was appointed the head of Sberbank in November.) Over the past eight years, the Center has been the center of economic legislation drafting or has contributed to drafts of Putin's key reforms, including the flat tax, land privatization, pension reform, health care, benefits monetization, and the public private partnership initiative. While reform momentum slowed two years ago and the CSR's role in economic policy-making diminished, Yudaeva said the center remains influential. For instance, she noted that Elvira Nabiullina, another former head of CSR, was appointed MEDT Minister in September 2007.

13. (SBU) Yudaeva said CSR is currently working on a number of projects for the MEDT, the Ministry of Regional Development, Sberbank, and the Development Bank. In addition, she noted that she and CSR president Mikhail Dmitriev sit on a number of government commissions, such as commission on administrative reform and corporate governance, to emphasize the close working relationship between the GOR and CSR.

14. (SBU) According to Yudaeva, her staff is currently working with the MEDT on the preparation of a new long-term economic strategy paper. However, she said the paper would be more of a comprehensive overview of economic trends instead of a new strategy on economic development. The Center is also working closely with newly-appointed Minister of Regional Development Kozak. In April, while still Southern polpred, Kozak approached her to work on an economic development strategy for the Southern District. Since Kozak's new appointment, the project has expanded to include drafting of an economic strategic plan for all seven federal districts. She added that the Ministry will not allocate a single kopeck for development projects in any of the seven districts until each district presents a strategic development plan.

15. (C) Yudaeva said CSR is also conducting research for Sberbank, now that Gref has been appointed as its head, and is working with the newly created Development Bank. Yudaeva said that the deputy director of the Development Bank, Sergei Vasiliev, is a close colleague.

16. (SBU) In response to a question about CSR's sister organizations in the regions, Yudaeva said that the Moscow CSR office has no relationship with these regional think tanks that use the CSR moniker and that her office often

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competes with these other offices on various projects.

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Russia's Competitiveness and State Corporations  
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17. (SBU) Yudaeva talked about the competitiveness research project that CSR started at the beginning of 2006. Then-MEDT Minister Gref hired Harvard academic Michael Porter to conduct research on Russia's competitiveness vis-a-vis other countries. On November 22, CSR conducted a seminar with presentations prepared by Harvard University professors Michael Porter and Christian Ketels. The report, which can be found on CSR's website, presents an overview of Russia's competitiveness vis-a-vis the rest of the world.

18. (SBU) In addition to high oil prices, the report highlighted the ruble devaluation and unused production capacity as factors behind much of the economic growth from 1998 to 2004. However, these factors had been exhausted by 2004 and Russia's competitiveness has started to decline. The report noted the GOR's failure to take advantage of Russia's macroeconomic stability to implement reforms, such as overhauling the health care and educational systems, to increase competitiveness and diversify the economy.

19. (C) Yudaeva commented that Porter's reports have generated mixed reactions from the MEDT. For example, MEDT Director of Forecasting Andrey Klepach, criticized the report for not offering any new ideas. He also criticized the report's reliance on international indices and rankings, which fail to capture important nuances in the trends. MEDT Deputy Minister Androsova, on the other hand, was quite pleased with the report because the MEDT could use it to support its position in internal GOR debates on economic policy.

110. (C) Yudaeva said that, in general, she agreed with the conclusions in the report especially its criticism of the state's growing presence in the economy. She admitted that little could be done about this shift, in particular given the many vested interests in the Kremlin surrounding the push

to create state corporations. For example, she said that Chemezov's ambitions were the sole reason behind the recent creation of Rostekhnologiya, the defense sector holding company that will absorb arms exporter Rosoboronexport and a half a dozen other defense sector companies.

¶11. (SBU) Yudaeva said that another reason for the GOR's preference in relying on state corporations to address everything from shipbuilding, housing, and the nuclear industry to preparing for the 2014 Winter Olympics in Sochi, is its frustration that the privatization drive in the 1990's has not revived Russia's manufacturing base. She said the GOR wanted faster results and guarantees. She added that the Russian mentality, shared by the population and government officials alike, to trust authority figures over private agents, also contributed to the shift in economic policy to the state corporation model.

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Post Putin Economic Policy  
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¶12. (C) Turning to economic policy after the March 2008 presidential elections, Yudaeva commented that economic policy would most likely continue without significant change with a new president. She said that only external factors could lead to a significant change in economic policy. For example, a large drop in energy prices or some other external shock might lead to an economic policy course correction.

¶14. (C) Yudaeva appeared resigned to the fact that the GOR has chosen the state corporation model to solve its immediate economic problems. She said there were cycles in Russia's economic policy history with periods of centralization and decentralization following one another. The trend towards centralization would eventually make way for more liberalization. In a few years, for instance, she predicted that the GOR would liberalize the gas sector with semi-autonomous companies allowed to operate side by side with Gazprom.

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¶15. (SBU) When asked whether any of the presidential hopefuls are creating think tanks similar to Putin's creation of CSR in 1999 when he became prime minister, Yudaeva commented that the economic environment was completely different in 1999. At the time, the country was in the midst of an economic crisis and drastic measures were necessary, but now, there was no urgency. She added that other economic think tanks are positioning themselves as CSR's successors, but she claimed they are not presenting any new ideas (reftel).  
BURNS